Can cash and trade be a marriage made in heaven?

A recent SWIFT panel session moderated by *TFR*'s **CLARISSA DANN** discusses the convergence of cash and trade debate and client/bank symbiosis in unlocking working capital

Q1. What do we mean by the convergence of cash and trade? Is it a buzzword and does it mean different things for banks and corporates?

KAH CHYE TAN. I believe that cash and trade has always been converged but where does it converge? Recent history suggests this is a bank-led debate and that it converges at the level of the relationship manager who owns the cash and trade solutions. I think that will continue to exist in many banks.

CLARISSA DANN. In other words there is convergence in roles?

KAH CHYE TAN. A lot of this depends on the evolution of the bank and on its strategy. There is not a right and wrong answer. You can converge at the GTS level or at the relationship level. The key is not losing the expertise of trade or cash because the client comes to us for that expertise.

ADNAN GHANI. Is this a marriage of convenience or a match made in heaven? My first view was this is a marriage in hell but I have changed my view. Kah Chye is right, banks have tried different models for different segments – they have bundled and unbundled themselves. Traditionally there has been the product-led model or

THE PANEL

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Alexander Malaket's reaction to Kah Chye Tan's insistence that SWIFT could do more with trade messaging

the generalist-led model and banks have usually been somewhere in between. And it depends on the segment you are servicing. With a mid-market or SME client, the person acting as the CFO or treasurer and purchasing manager is one set of people. This clarity and focus in the mid-market is a huge opportunity for operational effectiveness. But the larger client is struggling with alignment and you typically have a logistics department, purchasing department, treasurer, CFO and sales in different places.

CLARISSA DANN. One banker said that when he went in to see a large corporate client he ended up introducing different departments to each other as they hadn't met before![1]

ALEXANDER MALAKET. I know which one you mean! We can look at the question of convergence at a strategic level: what is the business of the bank doing what does it look like how does it align with the business in the various client segments the bank responds to?

And then there is the relationship level: how are the relationships being managed, are they owned by separate relationship managers or is that function within the bank integrated? How does that align with the client contacts managing the finance and treasury functions? The third level is the operational transactional level: how do you do the deal, what that means operationally and how you deal with process flows? I think there are different levels of development of convergence flows across all three of those dimensions across different financial institutions.

Q2. Shall we take a closer look at working capital management and the how that strategy plays out by looking at a holistic approach to transaction banking

KAH CHYE TAN. If you are talking about a smaller segment client, cash and trade always converged because, as Adnan says there is one point of contact within the client's organisation that is responsible for all the cash and trade inflows and outflows. You get the silos in large corporates and large banks and I don't see material changes in these large organisations in the foreseeable future.

ADNAN GHANI. A report from one consultancy says that that if companies could get their working capital cycles correct, up to US$750bn trapped working capital could be released. In another study 57% said they were focusing on working capital to generate more cash so when the cycle turns more positive they have the cash available for opportunities. They are realigning themselves and using their ERP systems to access data to help them forecast and manage their future cashflows, foreign exchange (FX) needs and counterparty risk. In turn, as banks focus on their clients, they are also rebundling themselves to present a working capital solution to the client. It's not easy to bring cash and trade together – yes they might sit together or report to the same person, but that doesn't mean you have brought anything together for the client. You could merge into one unit, and typically trade will learn a bit of cash, cash will learn a bit of trade but neither are comfortable presenting the nuts and bolts of either solution so you can end up giving a mixed message to the client. Revenues would fall. Of course if banks get it right, there is a big prize at the end but there are challenges. Even if you have the all-singing all dancing technology with single sign-on, single data entry, cash and trade forecasting functionality, FX, payments receivables etc, you need trained experts in trade or cash. You have to reboot yourself.

Q3. Does this mean that banks have to act as consultants themselves?

ALEXANDER MALAKET. I absolutely think in the trade space and in transaction banking there is a tremendous store of expertise in banks that is underleveraged and undervalued. That undervaluation of the business is a devaluation of the expertise in financial institutions. One of the encouraging trends is that banks are talking about taking a more expert adviser role and that is a positive development for the industry – and serves clients better.

KAH CHYE TAN. I think this is already happening and at the top end of the market it is true that banks are nudging the corporates to converge. But the bank needs to take a more pragmatic approach and converge only where it makes sense. Look at technology and internet banking which is fully converged.

When trade works with cash management colleagues, they can take the accounts payable file – which is already in the bank – and tell the client how they are going to provide finance for it, or how they are going to discount the receivables. Half the business is already in the bank, so why not get the other half?

Q4. How do you overcome the challenge where somebody has to see right across the departments?

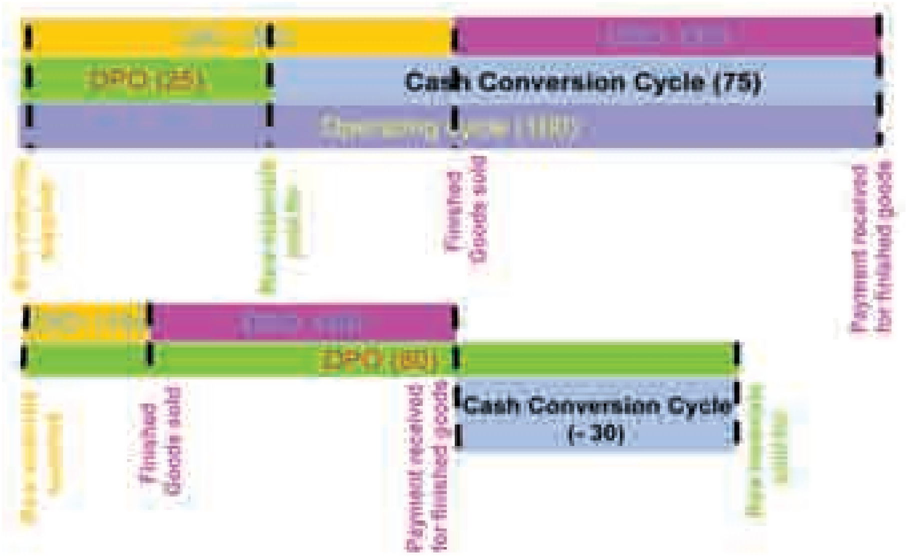
KAH CHYE TAN. I believe that the solution lies not just in the technology or organisational structure but in building the right culture to get cash, trade and FX colleagues to work effectively with each other in good partnerships.

Q5. What more can be done to release this working capital locked up in the system?

ADNAN GHANI. I want to pick up on the consultancy role of banks. Only yesterday I was having a meeting with the treasurer of a large media corporate and he said: "Adnan, what I really need from a banker is to get under the skin of our operation and understand what we do. And then pitch us ideas – we love ideas about how we can improve things. What we tend to get instead is people throwing products at us and hoping something will stick." For me, this puts into perspective about what we should be doing as a banker as a trusted adviser. In terms of releasing working capital, the research highlights that if all the companies were to become best in their class at working capital management around US$750bn would be freed up. It's not rocket science for banks to look at a client's DSO, DIO and DPO and advise on a supply chain finance solution (see Figure 1).

Kah Chye touched on cross-sell opportunities for banks. It is well known that if I am providing a payables SCF to my suppliers and I am discounting those invoices – if the supplier leaves those deposits in my account, I make more money in cash management than if I am providing a trade solution. Similarly, if I am settling something in trade I am making a payment – typically in two currencies – so there is probably a FX cross-sales opportunity. The client needs a package or it's like getting your burger from McDonalds and then crossing the street to Burger King for fries and cola!

Figure 1: Summary of cash conversion cycle



From a working capital perspective, cash and trade clearly converge in their impact on the cash conversion cycle (Days Sales Outstanding (DSO) + Days Inventory Outstanding (DIO) – Days Payables Outstanding (DPO)). It is estimated that companies that optimise their cash conversion cycle can reduce their working capital requirements by as much as 35/40%

Source: SWIFT

ALEXANDER MALAKET. One Turkish corporate told me that when the banks come to visit all the presentations are interchangeable and what he wanted was solutions to his problems. Clients complain to me that they perceive a certain mystique in the trade business and I have heard cash people say: "Why do you make it so mysterious so those of us not in it cannot learn it?"

Q6. Are there any shining examples who have said 'yes – these are the solutions we have been looking for"?

ALEXANDER MALAKET. The driver behind supply chain finance and cash/trade convergence was the risk the banking sector faced of disintermediation in the trades space when importers and exporters were gravitating to open account terms once LCs were perceived as too expensive and complicated. But imagine your banking business tomorrow if trade disappeared – a huge amount of FX business is driven by trade.

KAH CHYE TAN. That is very true. Trade does facilitate a lot of FX and our FX colleagues benefit from trade transactions. But as clients move from LCs to open account, we have to work very closely with our cash colleagues or the FX business will be lost. And I do believe clients buy product expertise. If you have a heart problem you want a heart surgeon to open the heart, you don't want a general practitioner. It's all very well to say we want one person to sell multiple solutions but when you have a real problem to solve you want an expert – so balance is important.

ADNAN GHANI. Balance is important but the earlier question about whether banks are providing a consultative approach is important. Banks are struggling with this. We are all the same space, and we are investing in skills to give more options to clients.

> **"You get the silos in large corporates and large banks and I don't see material changes in these large organisations in the foreseeable future"**
>
> KAH CHYE TAN

ALEXANDER MALAKET. There is one institution in Europe that is working very much in the spirit you described and is taking away product ownership from the relationship managers and telling them to go away and figure out, as consultants, what kind of solutions clients want.

Q7. So what is the outlook for cash and trade convergence over the next three to five years?

KAH CHYE TAN. It will continuously evolve.

ALEXANDER MALAKET. Yes cash and trade are the two key elements underpinning discussions about the development of global transaction banking.

ADNAN GHANI. It is a match made in heaven and the way both corporates and banks are heading.

Questions from the floor

Q8. Does the panel think the current economic conditions will speed up this convergence because people looking for economies of scale?

ADNAN GHANI. Yes. One of the main determinants of why larger corporates are looking at working capital and aligning themselves so they have end-to-end view on cash and working capital cycles is because of the economic situation. As banks we are led by our clients and are responding to this.

RENE CHINNERY (head of supply chain finance at Lloyds TSB Commercial Finance, speaking from the floor). I was in a meeting, onboarding a major corporate supplier to a supplier finance programme selling into a major corporate buyer and the finance director told me – which I found interesting – "Rene, do you know what, I had access to finance for this transaction at the same or a better cost than you are offering me but the reason I am signing up with you is what you are offering me totally integrates the way I do business with this customer." So I would like the panel's view on the efficiencies we are delivering to our customers.

Clarissa Dann and Adnan Ghani talk about marriages made in heaven

KAH CHYE TAN. This is very true. As banks we help with a set of processes, we provide information, liquidity, and we mitigate the risk. Whether the economic crisis is forcing clients to focus on liquidity driving this integration, they are a lot more cost conscious now. And cost pressure will only increase. This translates into an increased demand for operational efficiency. So the more we can model our banking services after the financial supply chain, the better off we are in serving our clients.

Q9. We all talked about integration of relationships. How do you see convergence from a technical point of view – in terms of cash, FX and trade?

ADNAN GHANI. In a recent RBS survey 40% of all respondents said they would like a multibank diagnostic solution where cash and trade is all integrated. Within a bank there are multiple legacy systems and trying to bring this into one has been a costly challenge. But it can be done – you start with a single sign on and work your way through the system.

CLARISSA DANN. What is the role of SWIFT in all of this?

ALEXANDER MALAKET. The development of trade services utility (TSU) and bank payment obligation (BPO) has been an important natural evolution of doing business and SWIFT has been careful to engage in the industry developing a solution.

KAH CHYE TAN. I think SWIFT could do a lot more. We are so far from an acceptable level of integration as far as technology is concerned. SWIFT has done a great job on the cash side of the business and a lot of the expertise it has done developing cash standards could be transported to the trade side. We need to be a lot more structured and a lot more disciplined with our trade messages on the SWIFT side. The banks are not without blame here. We keep telling our clients – I am being self critical – we are this multibanking platform. Where does this begin and end? It begins with a common user ID and ends with a password.

Reference:

1. A remark made by Chris Bozek of Bank of America in the SWIFT e-invoicing panel session at Sibos. See www.tfreview.com/face-to-face/treasury-management/visible-payment-line-e-invoicing